

WILEY

**Written Statement of
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before the

**Subcommittee on Courts, Intellectual Property and the Internet
Committee on the Judiciary
United States House of Representatives**

FIRST SALE UNDER TITLE 17

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Mr. Chairman, Ranking Member Nadler, Members of the Subcommittee, thank you for this opportunity to testify before the Subcommittee on the subject of the first sale doctrine in U.S. copyright law.

I am Stephen Smith, President and CEO of Wiley. Founded more than 200 years ago, Wiley has evolved from a small, family-owned printing shop to a publicly-traded global publishing corporation with revenues of \$1.8 billion in which the Wiley family still retains a controlling interest and leadership of its independent board of directors. Headquartered in Hoboken, New Jersey, we serve customers in 211 countries and territories worldwide. We have 5500 employees worldwide including facilities and employees in Massachusetts, Florida, Indiana, Iowa, Arizona, Texas, Colorado, California, Minnesota, Illinois and Virginia.

Our core mission is to educate communities around the world through our publications, technologies and content-enabled solutions. Our knowledge and knowledge-enabled products and services improve outcomes in Research, Professional Development and Education.

Through our Research segment, we provide digital and print scientific, technical, medical and scholarly journals; reference works; books; database services; and advertising. Our Professional Development segment provides digital and print books, online assessment and training services, and test prep and certification. In Education, we provide print and digital content and education solutions, including online program management services for higher education institutions and course management tools for instructors and students.

We are a global company with operations around the world. Our ability to operate effectively in the global marketplace depends heavily on the protections provided by copyright law in the U.S. and in foreign markets. The copyright system plays a significant role in fostering investment in the development of new content, underpinning innovation and economic growth.

THE FIRST SALE DOCTRINE

The proper application of the first sale doctrine represents a crucial component of copyright law. It places a clear, but narrow, limit on the copyright owner's right to control the subsequent distribution of a lawfully-made physical copy of a work. This generates a number of important consumer benefits that Wiley supports, including lending and resale of such physical copies of published works. When properly applied, it also avoids interference with a copyright owner's importation rights in order to ensure that authors, publishers and other distributors of works that depend upon copyright in making these works available to the public can operate effectively in the full range of industrialized and developing world markets by implementing market-appropriate price differentials.

In 1976, intending to redress the impracticability of the unitary copyright and to create the ability for copyright owners to license separate limited rights in an original work, Congress enacted amendments to the Copyright Act to establish the principle of divisibility, along with prohibitions on unauthorized importation. In doing so, Congress established the predicates for market segmentation, allowing U.S. content owners to manage their rights efficiently by allocating them to different markets, with the understanding that the economic interests of the copyright owner are endangered if they cannot be exercised on a territorial basis. Price differentials arising from economic differences among countries are necessary to facilitate participation in diverse markets.

Both the foreign buyer and the U.S. seller benefit from market segmentation. Consumers overseas can purchase copies of copyrighted works that they value at a price that is reasonable for their market. The U.S. seller gains effective access to a market which would otherwise not sustain an unsuitably higher price point.

In the U.S., the first sale doctrine – historically implemented alongside and consistent with these key concepts – did not hinder or prevent such participation in global markets and allowed the benefits of such participation to flow not just to the publisher, but to the entire value chain that creates and markets high-quality content. This chain includes skilled authors, artists, researchers, editors, production workers and marketers, in high-paying jobs that are the hallmark of our industry. Moreover, the proper application of the first sale doctrine benefits U.S. consumers as well by allowing U.S. copyright owners to recoup their investment and to extend production costs over a broader number of transactions, thereby helping to contain price increases.

The benefits are not limited to economic advantages that accrue to content creators, providers and consumers. They include less tangible but equally important social benefits that result from disseminating our high-quality and innovative content and technology. This is especially true in the case of underserved populations who would not have access to our products if we could not use local prices. We foster the global dissemination of knowledge by making our products legally available at local prices. And we believe that by doing so, we enhance the global reputation of the United States as a primary source of leading-edge, knowledge-based content.

The social benefits of market segmentation are an especially important feature of our educational products. Price differentials allow us to make legally available to students around the world materials which reflect U.S. cultural, social and political values, exposing successive generations of emerging leaders to this country's vision of a just, peaceful and prosperous world.

THE IMPACT OF *KIRTSAENG V. WILEY*

These aspects of the U.S. copyright system, which have enabled U.S.-produced copyrighted works to so richly benefit the U.S. economy by becoming the most successful category of

exported U.S. products in our national export-import balance of trade,¹ were seriously undermined by the U.S. Supreme Court's split ruling in the case of *Kirtsaeng v. Wiley* in March of last year. A Thai national came to the U.S. in 1997 for university studies. While living in this country, he asked his relatives in Thailand to purchase Wiley Asia's English-language textbooks in Thai bookshops and ship them to him in the U.S., where he sold them for a profit. Printed warnings in Wiley Asia's books state that they are not to be taken into the U.S. without our permission.

In 2008, we filed suit against this illegal importation of copyrighted works. After our suit was successful in both the federal district court and court of appeals in New York, the case was eventually appealed to the Supreme Court.

In March 2013, the Court, in a split 6-3 decision, ruled that the unauthorized importation and resale of copyrighted works manufactured and intended for distribution only outside the U.S. was permissible under Sections 109(a) and 602(a)(1) of the Copyright Act. The Court's ruling destroyed a copyright owner's importation rights, creating new barriers for them to overcome in order to successfully compete in global markets.

We believe that the majority opinion in this case is inconsistent with Congressional intent, longstanding U.S. trade policy and the Court's own established practice of deferring to Congress on copyright policy.

The *Kirtsaeng* decision broadened the traditional scope of the first sale doctrine's effect from "national exhaustion" to "international exhaustion" of the copyright owner's distribution right regarding physical copies. By adopting an international exhaustion regime, the U.S. has broken from conformity with the policies of trading partners where the sale of a physical copy of a

¹ *Copyright Industries in the U.S. Economy: The 2013 Report*, by Stephen E. Siwek of Economists Incorporated, prepared for the International Intellectual Property Alliance (IIPA), November 2013.

copyrighted work outside their country does not exhaust the copyright owner's distribution right. This has created confusion and disruption in the global marketplace, lessening the availability of our products and placing us at a competitive disadvantage. As a result, the Supreme Court ruling creates a disincentive for U.S. publishers to participate in foreign markets.

In effect, the Court's ruling in favor of "international exhaustion" encourages and facilitates international arbitrage in copyrighted products, which undermines a copyright owner's ability to segment markets and establish necessary price differentials. This has unintended, adverse consequences.

In educational products, for example, allowing the importation into the U.S. of textbooks produced abroad for an overseas market is not leading to lower costs for students. Instead, publishers have either withdrawn from certain international markets completely or are obliged to work with fewer, more trusted distributors, thus lessening the availability of legitimate versions of their products in underserved foreign markets and reducing the overall number of transactions through which they can recoup their various production and dissemination costs. To prevent arbitrage, some publishers are now only offering their products abroad at higher, non-local prices which students cannot afford.

The Court's rewriting of the law in *Kirtsaeng* is also leading to a disturbing increase in piracy, another unintended consequence. As publishers lose the ability to supply non-pirated content on a price-to-market basis, former overseas customers turn to counterfeiters to fulfill their needs at prices that are sustainable in their economies. This causes a palpable increase in print piracy outside the U.S. and a higher incidence of those copies being sent into the U.S.

In addition, the ruling places upward pressure on prices. At Wiley, in order to maintain our ability to successfully participate in foreign markets, we have invested more heavily in International Student Versions (ISV) of our products. These products may be organized differently, contain different problem sets or contain other material content differences.

Preparing these products and producing a separate version of a book for the international market substantially increases our editorial, production and other costs. These higher costs, when added to the loss of foreign sales revenue, lead to higher U.S. prices. Moreover, students and educators around the world often want the U.S. version of the work, not a special international version.

Notably, two members of the Court who participated in the majority opinion in *Kirtsaeng*, Justices Kagan and Alito, indicated in their separate concurring opinion that the ruling was essentially required, based on the Court's earlier ruling in *Quality King Distributors, Inc. v. L'anza Research Int'l, Inc.*, 523 U.S. 135 (1998), which held that the first sale doctrine limits the applicability of the Copyright Act's prohibition against unauthorized importation, and thus led the Court in *Kirtsaeng* to "unavoidably diminish" the scope of that prohibition and "limit it to a fairly esoteric set of applications."

They explained that, had the earlier decision come out the opposite way, it would have permitted a copyright owner to restrict the importation of copies irrespective of the first-sale doctrine, enabling the copyright owner to segment markets through price differentials without imposing down-stream liability on libraries or others who purchase and resell in the U.S. physical copies of the works that were manufactured abroad. Their concurrence, along with the dissenting opinion of Justices Ginsburg, Kennedy and Scalia, invites Congress to clarify the importation right and reaffirm the traditional interpretation of the first sale doctrine's effect as being one of national exhaustion, not international exhaustion.

Consistent with the concurrence of Justices Kagan and Alito, Wiley recommends that Section 602(a)(1) of the Copyright Act (as amended) be revised to clarify that "importation" is not simply a synonym for "distribution," and that the copyright owner's right to control importation is a critical aspect of U.S. international trade law and policy which, unlike the right to control the distribution of copies within the U.S., is not subject to the application of the first sale doctrine. Importation is a distinct type of distribution and an action that should be regulated

under the Copyright Act without limitation by the first sale doctrine. That is because Section 109, which codified the first sale doctrine, deals with selling or otherwise disposing of copies, but does not address importing them.

The reference to Section 106 in Section 602(a)(1) should be eliminated so that the language would make clear that the unauthorized importation of copies that “have been acquired outside the United States is an infringement of the copyright owner’s right to import or authorize the importation of such copies or phonorecords.” The first sale doctrine would then, as a general matter, apply to copies “lawfully made under this title” without regard to the place of their manufacture, whenever the owner of such copies sells or otherwise disposes of possession of them. It would not provide a defense, however, to the unauthorized importation of such copies.

In Section 602(a)(3), Congress provided for exceptions to the right to control unauthorized importation, such as importation of copies “for private use” and “not for distribution,” in order to avoid adverse impacts on certain U.S. importers. The *Kirtsaeng* decision renders these exceptions essentially meaningless, since they are now subsumed in the new “rule” that non-pirated copyrighted works manufactured and sold anywhere in the world can now be imported into the U.S. without limitation.

Congress could consider whether reasonable limitations and exceptions, in addition to those already set out in Section 602(a)(3), are necessary and appropriate to mitigate concerns about possible adverse impacts on, for example, libraries and museums in the U.S., while still providing copyright owners with the legal basis for managing unauthorized importation that was the entire purpose of Section 602(a)(1). It should be noted, however, that the concurring opinion of Justices Kagan and Alito explains that such a clarification, as recommended above, would “target unauthorized importers alone” and not the libraries, used-book dealers, technology companies, consumer-goods retailers and museums whose asserted “parade of

horribles” that might have resulted from a contrary ruling so significantly influenced the majority opinion and the Court’s split decision.

Although the specific issue considered in the *Kirtsaeng* case was whether the reference in Section 109(a) to copies “lawfully made under this title” carried with it an implied geographic limitation to copies made in the U.S., Congress need not change Section 109(a) to expressly create such a limitation. While that would have the desired effect of reinstating the right of copyright owners to control unauthorized importation of at least some copies of their works, it could have unintended consequences, including providing an incentive for U.S. entities to manufacture their products outside the United States. Instead, changes to Section 602(a)(1) can accomplish the goal of restoring meaningful rights to control unauthorized importation without creating such risks.

At Wiley, we have succeeded in developing markets around the world for knowledge-based content which educates communities and disseminates this country’s values. The expansion of the effect of the first sale doctrine from national exhaustion to international exhaustion severely disrupts ongoing operations, undercuts decades of investment and limits our potential to expand our global footprint. I urge Congress to return the U.S. copyright system to its pre-*Kirtsaeng* state by clarifying longstanding Congressional intent through an amendment to Section 602(a)(1) of the Copyright Act.

DIGITAL FIRST SALE

The expansion of the effect of the first sale doctrine from national exhaustion to international exhaustion is causing unintended adverse consequences for buyers, sellers and creators of content in tangible forms, such as books. There are also proposals to extend the first sale doctrine to digital copies of copyrighted works, ignoring widespread market trends and consumer preferences favoring access rather than ownership models, as well as the critical differences between physical and digital copies.

Wiley believes that creating a “digital first sale” would undermine existing businesses and halt the development of new businesses that use licensing to offer consumers an unprecedented variety of ways and price points for accessing and using creative content.

For example, in 2007, Wiley and four other key education publishers (Cengage Learning, Palgrave Macmillan, McGraw-Hill and Pearson) founded CourseSmart to offer students, teachers and educational institutions new ways to access digital textbooks anytime, anywhere, in the form of short-term rentals, customizable coursepacks and accessible formats, all at significantly less cost than the traditional purchase of a physical copy of the work.

A digital copy of a textbook has significantly different properties than a physical copy. Whereas the transfer of a physical copy of a book places that book in the hands of the recipient and leaves the original owner with no copy, perhaps requiring time and money, the transfer of a digital copy can be instantaneous and virtually costless. Moreover, once transferred, the physical copy will deteriorate over time, and will deteriorate more quickly the more often it is used, whereas the digital copy does not deteriorate. There is no difference between a new and a used digital copy: they compete directly in the marketplace. Lastly, producing multiple copies of a physical book would be time-consuming and expensive, but reproducing a digital copy takes little more than the click of a button.

This is true despite the claims that there are technological means of ensuring that the party who transfers a digital copy immediately deletes it and retains no copies. A robust technology of this sort would be difficult to develop and police, without seriously intruding on personal privacy, and would likely be continually subject to circumvention in the rapidly evolving digital realm.

License-based business models like CourseSmart pass the benefits of digital course materials, such as portability and durability, on to consumers such as students and teachers in a variety of

cost and access models that would be significantly undermined, if not impossible to sustain, under an ownership-based model subject to the digital first sale doctrine.

In 2001, the Copyright Office produced a report for Congress analyzing the first sale doctrine in detail, including the implications of extending it to digital content transferred electronically. The Office concluded that the first sale doctrine should not apply in the digital world because doing so would unreasonably jeopardize copyright's fundamental goal of promoting the creation and dissemination of new content. That conclusion remains valid.

I recommend that Congress reject any proposal to extend the first sale doctrine to digital copies, in order to guard against adversely impacting thriving new digital markets and business models and inhibiting the development of new ways to disseminate digital content to users.

Thank you.